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November 29, 1993

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

BY HAND DELIVERY

Alexandra Wilson
Cable Services Division
Federal Communications Commission
2033 M Street, N.W.
Washington, D.C. 20557

Re: Practical Problems with Form 393 Instructions and Related FCC
Clarifications
Ex Parte MM Docket 92-266

Dear Ms. Wilson:

The National Cable Television Association hereby presents certain practical problems with Form 393 instructions and related FCC clarifications, and suggested solutions which pertain to both outstanding Petitions for Reconsideration and to the Third Notice in this Docket.

As the Commission is aware, most cable operators sought to bring their systems into compliance with the rules implementing the rate regulation provisions of the 1992 Cable Act by revising and restructuring their services and rates prior to September 1, 1993. The FCC actively encouraged the cable industry to voluntarily reduce and restructure rates to regulated levels. It adopted a general preemption of local and federal notices to

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facilitate the implementation of new rate and service offerings prior to September 1, 1993. The expectation that cable operators could and would bring their systems into compliance prior to September 1, 1993 also is evidenced by Congress' interest in the restructuring efforts and by the Commission's survey of restructured rates. The initial results of that survey clearly indicate that significant efforts have been made by the cable industry to reduce rates in anticipation of the new rules, thereby benefiting cable subscribers.

In undertaking the above-described efforts to restructure and reduce rates, cable operators necessarily relied on such information as was available to them at the time. As a practical matter, inflation data, equipment-related costs, channel lineups, and other factors relating to the rate calculation were "locked in" in Mid-August, as systems endeavored to compute their permissible rates and notify their subscribers (by mail, on-screen announcements, and newspaper advertisements) of the channels.

Cable operators generally expected the rates established as of September 1, 1993 to be the rates that they would have to defend once the process of regulatory review commenced. Because that review process could have commenced as early as September 1, 1993 for cable programming service tiers (and October 1, 1993 for basic service), operators also expected that rates properly calculated as of September 1, 1993 would be approved, thereby obviating any refund risk. As discussed below in greater detail, however, circumstances largely beyond the control of the cable industry have thrown the validity of the cable industry's restructuring and repricing efforts into doubt and threaten to create arbitrary distinctions in the treatment of various systems. The Commission can and should clarify and/or modify its rules so as to prevent these unanticipated and arbitrary results.

I. Minor Changes Between September 1 and "Initial Date of Regulation"

A. Changing Inflation Indices

As cable operators restructured and reduced rates in mid-August, they generally relied on the then-available GNP-PI figures of 124.1 ('93/2) and 121.8 ('92/3). The Commission is well aware that the Department of Commerce changes the figures for GNP-PI on a regular basis. The changes are both prospective and retroactive. While some operators may have learned that Commerce changed the GNP-PI numbers on August 31, 1993, it was too late for cable operators to change the rate calculations. Announcements had already been prepared, written bill inserts printed and often placed in the mail, marketing material had been revised and printed.

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On November 10, the Commission announced that for filings due November 15, the new inflation numbers should be used in lieu of the figures embedded in the Form 393. As noted in Continental Cablevision's November 15 petition for reconsideration of that action, the Commission's pronouncement has created enormous uncertainty regarding the status of rates that, as originally calculated in mid-August, were entirely proper. Moreover, given that the Commerce Department revises GNP-PI data on a regular basis, the confusion facing the cable industry (and local regulators) is likely to be exacerbated in the future.

Attachment A illustrates the effect of changing the GNPPI figures. An operator using the new numbers on September 1 would find that the rates just set were unlawfully high. However, the change in inflation creates only the appearance of excessive rates, depending solely on the timing of the "initial date of regulation." Attachment A shows that a rate set Sep. 1, 1993 using available GNP-PI information will be deemed unlawfully high (under the FCC's November 10 Q&A on inflation) for a filing made November 15. But the same rate will be at benchmark if the local government begins to regulate or the 329 is filed on Feb. 1, 1994. Thus, voluntary compliance with FCC rate rules will appear--with respect to complaints filed during a narrow three month window--to be unlawful overcharges. If a municipality certifies outside of that window, or a 329 is received after January, 1994, the rates will be more than justified.

The amount at issue can be a little as a penny, but if all marketing materials must be reprinted, all rates restructured, all billing reprogrammed, new bill inserts prepared, and refunds issued, the administrative costs are severe--and there is no mechanism for recovering those costs.

What is more, integrated community units served off of a common headend, with identical channel lineups and identical franchise fees, will be balkanized for ratemaking purposes. Part of the system will have maximum rates set at one level, part at another, based solely on the timing of the "initial date of regulation."

Moreover, the benchmark for basic may be different than the benchmark for CPS tiers, again based solely on when a franchising authority certified versus when a 329 was filed.

Beyond the impact on cable operators, the Commission's instruction regarding the inflation adjustment will greatly increase the administrative burdens associated with reviewing rates. Rather than simply testing the legitimacy of the rate established through voluntary compliance on September 1, 1993, the Commission will have to recompute cable

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programming service rates for each system that is the subject of a Form 329 complaint, and will have to review each local recomputation for the basic rate.

B. Change in "Refreshed" Data

The change in the GNP-PI figures is only one of the problems with present instructions. The November 10 clarifications, and informal discussions with staff, have indicated an assumption that data should be refreshed to the date of filing a Form 393. Another illustration will demonstrate some of the absurd results that compulsory refreshing will create.

Attachment A held equipment costs constant at zero for purposes of illustrating the impact on rates of the change in inflation. That, of course, is an unrealistic assumption for any system which incurs costs for installation and converters. Attachment B presents a system with not atypical investment in converters, and demonstrates the effect of the passage of time on the legitimacy of rates under "refreshed" filings. The only changes shown are the inclusion of inflation and the recognition of one more year's depreciation on the converters. The result shows that if a complaint is filed after books are closed at 12/31/93, then the program service rates are \$0.13 too low and the converter rent would be about \$0.20 too high—but there is no mechanism for adjusting the rates in the interim. In truth, the revenue stream is neutral either way—because it is capped at the "base rate," and merely distributed among equipment and program service charges by Form 393. But "refreshing" the data gives the appearance of overcharges on the converters. And while there are clear procedures in effect to require reductions in the equipment charge, price caps may prevent offsetting increases in the program service rates.

This is an artifact of the instructions, but the consequences are dramatic. Depending on when a complaint is filed at the FCC, compared with when a franchising authority asserts rate regulation, the same piece of equipment could have two prices, and the benchmark rate which is lawful for one tier would be unlawful for the other.

These variables are not the only one's that will change. We would also expect the number of subscribers, number of subscribers to each tier, and equipment revenue to change, creating still more artificial swings in the "lawful" rate.

II. Channel Changes Prior to the FCC's Adoption of a Channel Add/Drop Formula

As the Commission is aware, after September 1 many systems added channels,

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such as home shopping must carry broadcasters. Others have agreed to add new channels (such as ESPN2 or the Food Channel) prior to the end of the year. In its November 10, 1993 "Questions and Answers on Completion of FCC Form 393 and Associated Filing Requirements," the Commission stated that, in completing Form 393, "operators should use the number of channels as of the initial date of regulation instead of channels offered on a different date." (Question No. 6.) This suggests that channels added prior to the initial date of regulation should "count" as regulated channels on the Form 393 for purposes of calculating the initial benchmark. Channels added after that date are to be treated under a formula to be adopted shortly, but the recovery of charges justified by that formula are in question because of two limitations. First, programming "externals" are not treated as chargeable if they are incurred prior to the initial date of regulation. Second, except in those few communities which have sent "initial notices," rates remain frozen into mid February.

Although cable systems adding channels after September 1, 1993 expected that they would be permitted to adjust their rates upward to reflect the addition of a channel, the rate freeze and uncertainty as to how the "going forward" approach would work have effectively prevented any adjustments. Now, as it turns out, the Commission has decided that channels added after September 1, 1993 should not be treated as "going forward" channels, for which additional charges may be imposed, unless the channels were added after the "initial date of regulation." The initial date of regulation has not yet occurred, for either basic or non-basic, in most communities; moreover, the earliest possible initial date of regulation for basic service was October 1, 1993.

This present anomalies which are illustrated in Attachment C. For example, a system that added a home shopping channel to basic service before either the basic or non-basic tiers were regulated: (a) is unable, due to the price cap limits, to increase its basic service rate to reflect the increased level of service; and (b) will have to reduce its non-basic rate (and make refunds). The combined price should be higher, but the freeze and cap prevent recover of the charge for the new channel.

The Commission's approach creates an enormous incentive for local governments to delay the commencement of regulation; moreover, operators are unlikely to add channels to regulate tiers if they not only are precluded from increasing regulated rates to reflect the channels added but also have to reduce the rates charged for other tiers.

III. The "Good Operator" Problem

A final problem associated with the completion of Form 393 by systems that

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restructured their rates and services prior to September 1, 1993 involves systems that have voluntarily chosen not to set charges at the maximum permissible level for their service and/or equipment offerings. Under the Commission's benchmark formula, a system determines its maximum permitted service rate by combining its service and equipment revenues and deducting the cost of the equipment. If the system sets its service and equipment rates at the maximum permitted levels, re-completion of the Form 393 should validate the revised rate structure. However, if any component of the rate structure is set below the maximum level allowed, re-completing the Form 393 will produce a maximum permitted rate level that not only is lower than that produced by the initial run-through, but that also is lower than the rates being charged.

The problem is essentially an offshoot of the problem relating to Lines 301 and 104 discussed on Question Number 7 of the November 10 Questions and Answers. The solution, as hinted at in the Questions and Answers, is to permit operators to use the same information in determining that equipment revenues as used in determining their equipment costs.

IV. Summary

Thus, at a minimum, the Commission's present instructions on refreshing data has these bizarre consequences for operators who voluntarily brought their rates into conformity with FCC rules on September 1, 1993:

- Through passage of time alone, the apparent validity of the line 600 rate will change depending solely on the date of complaint.
- A cable operator can never set a lawful rate unless a complaint is filed in every community unit immediately after setting of that rate.
- Voluntary compliance will now look like illegal conduct, because rate recalculations will be different from September 1, 1993 rates.
- To reset rates requires reprinting all marketing & advertising materials, with administrative costs for rebilling and customer notices which may exceed the amount of the refunds.
- Integrated community units with identical characteristics will have different programming, converter, installation and other rates depending solely on timing of

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initial date of regulation.

- The FCC will need to recompute the rate for each 329, and on review of each appealed local rate decision, rather than testing the legitimacy of the rate established through voluntary compliance on September 1, 1993. The administrative burden will increase needlessly.
- Basic and tier per-channel rates will vary depending on timing of local versus federal regulation. The "cost-based" equipment rates embedded in a federal 393 will differ from the "cost-based" equipment rates embedded in a local rate case, even for the same piece of equipment.
- When rates are recalculated, there will be an apparent (but not actual) overcharge for some rates and an apparent (but not actual) undercharge for others. The overall revenue stream to the operator is neutral either way, but existing regulations suggest the need for a refund.

V. Solutions

There are some very simple solutions to these problems:

- Operators should be permitted to rely upon the data used to establish September 1 rates if they voluntarily restructured to meet FCC rate regulation.
- Data need not be refreshed for any complaints filed between September 1, 1993 and September 1, 1994.
- Operators who apply for inflation adjustments within the one year window would true up inflation to then current numbers.
- Programming added between September 1 and the adoption of a channel add/drop formula would be treated as subject to the add/drop formula, but not less than the amount chargeable if the services were added before the initial date of regulation and reported on the Form 393. In addition, the Commission should not allow the addition of a channel to one tier to affect the rates allowed to be charged for other tiers.
- Operators should be permitted to use the same information in determining Line 104 equipment revenues as is used in determining Line 301 equipment costs.

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Respectfully submitted,

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Enclosure(s)

ATTACHMENT A

EFFECT ON MAXIMUM RATE OF CHANGES IN INFLATION INDEX

Equipment Cost Held Constant at Zero

	Sep 1	Nov 15	Feb 1
Tier Charge BBT	\$6.40	\$6.37	\$6.42
Tier Charge CPS	\$17.59	\$17.51	\$17.66
Combined Price	\$23.98	\$23.88	\$24.08
Base Rate Per Channel	0.532948	0.530715	0.535034
Benchmark Channel Rate	0.512	0.512	0.512
GNP-PI Current	124.1	125.6	125.6
3d Quarter '92 GNP-PI	121.8	122.5	122.5
Inflation Factor	0.018883	0.025306	0.025306
Adjustment Time Period	13	13	16
Adjustment Time Factor	6	9	9
Time Factor	2.166666	1.444444	1.777777
Inflation Adjustment Factor	1.040914	1.036553	1.044988
Adjusted Benchmark Rate	0.532948	0.530715	0.535034
Base Rate Per Channel	0.532948	0.530715	0.535034
Equip & Install Cost (Monthly)	0	0	0
Channel Factor	225000	225000	225000
Cost Per Sub-Ch	0	0	0
Base Service rate per Channel	0.532948	0.530715	0.535034

Note: The change in Combined Price illustrates that a rate set using available GNP-PI information at Sep 1 becomes nominally unlawful if the initial date of regulation is Nov 15, 1993 but is lawful if the initial date is Feb 1, 1994

ATTACHMENT B

EFFECT ON PROGRAM SERVICE AND EQUIPMENT PRICING THROUGH PASSAGE OF TIME Equipment Priced at Cost; Books Close at 12/31/93

	Sep 1	Nov 15	Feb 1
Tier Charge BBT	\$5.20	\$5.17	\$5.23
Tier Charge CPS	\$14.29	\$14.21	\$14.38
Combined Price	\$19.48	\$19.38	\$19.61
Base Rate Per Channel	0.432948	0.430715	0.435834
Benchmark Channel Rate	0.512	0.512	0.512
GNP-PI Current	124.1	125.6	125.6
3d Quarter '92 GNP-PI	121.8	122.5	122.5
Inflation Factor	0.018883	0.025306	0.025306
Adjustment Time Period	13	13	16
Adjustment Time Factor	6	9	9
Time Factor	2.166666	1.444444	1.777777
Inflation Adjustment Factor	1.040914	1.036553	1.044988
Adjusted Benchmark Rate	0.532948	0.530715	0.535034
Base Rate Per Channel	0.532948	0.530715	0.535034
Equip & Install Cost (Monthly)	22500	22500	22320
Channel Factor	225000	225000	225000
Cost Per Sub-Ch	0.1	0.1	0.0992
Base Service rate per Channel	0.432948	0.430715	0.435834
Converter Cost	\$2.00	\$2.00	\$1.83
Converter Gross	96000	96000	96000
Accumulated Depreciation	75000	75000	94200 Note 3
Net Investment	21000	21000	1800
Maintenance Hours	100	100	100
HSC	25	25	25
Current Depreciation	19200	19200	19200
Return	2362.5	2362.5	202.5
Number of Units	1000	1000	1000
Annual Converter Costs	24062.5	24062.5	21902.5
Monthly Converter Costs	2005.208	2005.208	1825.208
Monthly Converter Charge	2.005208	2.005208	1.825208

Note 1: Rates set Sep 1 using available GNP-PI information would be deemed too high by \$0.10 if the initial date of regulation is Nov 15, but would be \$0.13 too low if the initial date of regulation is Feb 1.

Note 2: In this model, equipment is priced at cost. The most recent information provided in response to a complaint filed Feb 1 would reflect one more year's accumulated depreciation. Converter prices would be deemed "too high," and program service rates "too low." There is no apparent mechanism to adjust for this common problem.

Note 3: One more year's depreciation is reflected in books.

ATTACHMENT C

EFFECT ON MAXIMUM RATE OF CHANGES IN CHANNELS

Equipment Cost Held Constant at \$0.10

	Sep 1	Oct 6
Channels on Basic	10	11
Tier Charge BBT	\$6.21	\$6.63 Note 1
Channels on CPS Tier	20	20
Tier Charge CPS	\$12.43	\$12.05 Note 2
Combined Price	\$18.64	\$18.68
Base Rate Per Channel	0.621353	0.602616
Benchmark Channel Rate	0.693	0.675 Note 3
GNP-PI Current	124.1	124.1 Note 4
3d Quarter '92 GNP-PI	121.8	121.8
Inflation Factor	0.018883	0.018883
Adjustment Time Period	13	13
Adjustment Time Factor	6	6
Time Factor	2.166666	2.166666
Inflation Adjustment Factor	1.040914	1.040914
Adjusted Benchmark Rate	0.721353	0.702616
Base Rate Per Channel	0.721353	0.702616
Equip & Install Cost (Monthly)	22500	22500
Channel Factor	225000	225000
Cost Per Sub-Ch	0.1	0.1
Base Service rate per Channel	0.621353	0.602616

Note 1: Basic rate should increase, but is frozen by caps, tolling, and or freeze.

Note 2: CPS Tier Rate appears too high, but the number of channels is unchanged.

Note 3: Benchmark is reduced to reflect change from 30 channels/20 satellite to 31 channels/20 satellite.

Note 4: Results are calculated using inflation information used in August, 1993. The relative results are unaffected by using 125.6/122.5 for GNP-PI.